

MICROSOFT RESPONDS TO THE THREAT

92. Once it realized the threat the Internet and browsing technology posed to its operating system, Microsoft began an unrelenting, and in my view illegal, campaign to protect its monopoly. Microsoft's response to the competition by Netscape was two-fold: first, an attempt to divide the market and, when that failed, a campaign to eliminate Netscape as a viable browser company by systematically shutting down our distribution channels and by engaging in other predatory acts.
93. With regard to Microsoft's effort to divide the market with Netscape, it is important to provide a brief background of the relationship between the two companies. Netscape builds products that run on Microsoft's operating system. Like any independent software vendor, ("ISV"), we are engaged, even today, in ongoing communication with Microsoft and other operating system vendors to be sure our software functions properly with the operating system. We have both formal and informal contact, the latter often occurring at industry conferences. I had one such conversation at a Hambrecht & Quist Entertainment Conference at Snowbird with Dan Rosen who was then Director of Strategic Relations of Microsoft. I knew Dan prior to this meeting

at Snowbird because he and I had worked at AT&T, after the AT&T acquisition of McCaw Communications. The conversation Dan and I had at Snowbird was very casual and friendly. He explained to me that he was the Microsoft person responsible for forming strategic relationships regarding the Internet and communications technologies. Dan described to me the nature of some of the sorts of deals he had been working on at Microsoft. Based on our conversation, I believed future discussions might be fruitful. Dan and I agreed to continue our discussions at a later date. I believed my prior relationship with Dan and his position with Microsoft presented an opportunity to build some sort of productive relationship between the companies. I was definitely interested in having Microsoft as an ally, not as an enemy, and hoped this discussion was a step in the right direction.

94. After this first conversation with Dan, I believe I had a couple of telephone conversations with him. At the time, I was aware that others at Netscape were talking with Microsoft about the adoption of a security protocol that Netscape had developed, called SSL, and a security protocol that Microsoft was in the process of developing, called STT. As I recall, these discussions were not proceeding very quickly. I vaguely recall that Dan initiated conversations to help move along the security protocol discussions.
95. I have reviewed certain e-mails sent by Netscape management and members of our engineering team prior to a June 2, 1995 meeting I had at Microsoft,

regarding Netscape's efforts to develop a browser that would work well with the upcoming release of Windows 95. At least as early as March 19, 1995, John Mittlehauser, a member of our technical staff and one of our initial hires, was corresponding with Thomas Reardon, Microsoft's Technical Lead of the Windows 95 Networking Group, about Netscape's work on a Windows 95 browser. (MS98 0135438). On April 11, 1995, Marc Andreessen, one of Netscape's founders and the company's Chief Technology Officer, corresponded again with Thomas Reardon about Netscape's Windows 95 plan. (NET 000957-58). On May 31, 1995, Tom Paquin, Director of Netscape Client Products, summarized several telephone conversations he had with Mr. Reardon, including specific discussions about technologies that would or would not be part of Netscape's Windows 95 browser. (NET 000199-000203).

96. I am also aware that there had been some discussions between Netscape and Microsoft prior to the time that I joined Netscape. I believe that Jim Clark, then CEO of Netscape, Ram Shriram, Netscape's Manager of OEM Sales, and Mike Homer, Netscape's Vice President of Marketing, had talked to Dan Rosen and others at Microsoft in the fall of 1994. I am informed that those discussions related, at least in part, to Microsoft purchasing or licensing Netscape's Navigator code. I am aware that those discussions did not prove fruitful because Netscape was not interested in Microsoft's proposal, which

was to purchase the Navigator code for what Netscape considered to be a low flat fee payment.

97. I have also very recently learned that in late December of 1994, Jim Clark sent an e-mail to Dan Rosen and Brad Silverberg, Microsoft's Senior Vice President, Personnel Systems Division, attempting to renew efforts to discuss the possibility of Microsoft licensing the Navigator code, even though Netscape was aware that Microsoft had by then already licensed the Spyglass browser code. Jim Clark has described this as a moment of weakness. In December of 1994, unsure of how to direct Netscape's business after having invested a substantial amount of time and money in the company, Clark was already searching for someone to replace him as CEO of Netscape. Indeed, Clark and John Doerr, one of Netscape's principal financial backers, had contacted me in mid-1994 about being CEO. I had accepted a position on Netscape's Board of Directors in October to consider the possibility. I have also recently learned that Jim's e-mail stated his opinion that there was no money to be made in the browser market. Jim did not tell me or the Board of Directors about this e-mail, and his opinion proved to be wrong. Netscape had just released its first commercial version of the product on December 15, 1994, and by the end of the first quarter of 1995, Netscape already had earned over \$2 million in revenues from the browser alone. Although Jim expressed this opinion in late December of 1994, I already was developing a

contrary opinion. As the history of Netscape's browser revenue in 1995 alone demonstrates, I came to believe that significant revenue could indeed be generated from browser licensing. My opinion proved to be correct. Over one half of Netscape's 1995 revenues of approximately \$85 million dollars was earned through browser licensing.

98. In May of 1995, Dan Rosen raised directly with me the issue of some sort of strategic relationship between our companies. Dan raised that issue at a time when we were spending tremendous resources on developing a Windows 95 version of Netscape Navigator. Windows 95 was scheduled for release in mid-summer, and we planned on releasing a compatible browser simultaneously. However, we were having difficulty getting the necessary technical specifications and licenses from Microsoft. I agreed to speak further with Dan in order to resolve these issues and to try to build a working relationship with Microsoft, as we discussed at Snowbird.
99. During mid-May, 1995, Dan and I set up a formal meeting to discuss these issues. The issue of forming a relationship with Microsoft was discussed at length among the members of the Netscape executive staff during May. For what turned out to be good reason, a few members of my executive staff expressed concerns about being too open with Microsoft. Microsoft already had publicized its intentions to develop a competing browser, and thus some members of the executive staff were hesitant to disclose all the newly planned

features of the browser, particularly because, at this point, Netscape was counting on browser revenue to be a significant portion of its total revenue.

Netscape's browser revenue more than tripled from the first quarter of 1995 to the second quarter of 1995. We did not want, and could not afford, to compromise that revenue.

100. Despite those reservations, I agreed to meet Dan on June 2, 1995. Prior to the meeting we had some substantive discussions about Netscape's plans. In addition, I was aware that other people within Netscape were still trying to obtain the necessary technical information from Microsoft to design a retail version of Navigator that would work well with the upcoming Windows 95 release. At this point, the Navigator version for Windows 95 already had been released in a pre-commercial or beta form on the Web.

101. On June 2, 1995, I met with Dan, Nathan Myrsvold, Microsoft's Senior Vice President, Virtual World Group, and Paul Maritz, Microsoft's Senior Vice President, Consumer Systems Division. The meeting was cordial and explored possible areas of collaboration between the two companies. I recall that Microsoft principally was interested in getting me to consider adopting certain security protocols, incorporating into Navigator certain viewers that would enhance Microsoft content, and other technologies related to our browser. I also recall that Microsoft stressed some server issues, including the potential of packaging a Netscape server product with Microsoft NT. I

also recall focusing on our browser product. I told Dan, Paul, and Nathan that we were gearing up for a retail release of Navigator and that we were already quite happy with the revenue we were generating from browser licensing. At one point during the meeting I suggested that Microsoft distribute Netscape's browser, often referred to as "the client." Although I did not think that Microsoft would take me up on this offer, I wanted to stress the importance of the client to Netscape's business strategy. I also recall that Marc Andreessen had asked me to raise several issues related to both browser and server technology. I recall that Microsoft was receptive to Marc's ideas. I also told Microsoft that continuing to improve the client was consuming a large portion of Netscape's engineering resources at that time. Finally, I recall discussing the importance of enterprise software to Netscape. The meeting ended in a friendly fashion, and we agreed to meet again.

102. I drafted some brief notes of the June 2 meeting and circulated them to my executive staff. As was my practice, the notes focused primarily on what Microsoft communicated to me. I have recently reviewed my notes and to the best of my knowledge they accurately reflect what Microsoft communicated to me during the June 2, 1995 meeting. (NSMS 60813).
103. About a week after the meeting, Dan Rosen forwarded his notes of the meeting to me at my request. I read his notes and agreed that they generally comported with my recollection of the meeting in terms of possible areas of

collaboration. I have recently reviewed Dan's notes (NET 00209-12) and agree that they accurately represent a portion of the discussions at the June 2 meeting. In particular, the notes confirm my recollection that I told Dan, Nathan, and Paul that Netscape's direction included "selling lots of site licenses for browsers," and that Netscape would only waive the license fee for students and non-profit organizations. Moreover, the notes confirm that I informed Microsoft of Netscape's planned retail launch of Navigator. The notes also confirm that I told Dan, Nathan and Paul that Netscape's browser plans focused on the Windows platform. Finally, I informed them that I believed that Netscape's primary competitor was Lotus Notes, and not Microsoft. That was an accurate statement at the time, because Microsoft had not yet announced its intention to displace Netscape from the marketplace by creating its own browser, bundling it with the operating system, and shutting us out of numerous browser distribution channels.

104. In sum, at the June 2, 1995, meeting I clearly communicated to Microsoft that Netscape was investing great resources in developing its browser, particularly for the Windows 95 platform, that Netscape planned a retail release of the browser, and that Netscape intended to earn money from browser revenues. Indeed, much of the technology that Microsoft was advocating that Netscape adopt, in particular the viewers, related to the Netscape client.

105. After the June 2, 1995 meeting, Dan and I had several additional phone calls. The primary purpose of the phone calls was to set up a meeting with a larger group of people from both Netscape and Microsoft. The plan was that Microsoft would do presentations on the technologies they were interested in having Netscape adopt, followed by question and answer, and a further discussion of both parties' plans. Dan circulated a draft list of items to be discussed at the meeting (NET 000017-19). Marc Andreessen sent an amended list of discussion items back to Microsoft. (NSMS 51545) The amended list indicated items that we thought were most important. Our top priority was to obtain APIs and other technical information we needed from Microsoft in order to release a browser compatible with the Windows 95 operating system. As discussed below, I had been informed that we had been having difficulty getting timely and helpful responses from Microsoft personnel on these issues. We hoped that the meeting would solve these problems. The meeting was set for June 21, 1995 at Netscape.
106. **The June 21, 1995 Meeting – Microsoft Proposes Dividing The Market** – As discussed above, we needed certain technical data for our browser to be ready for release with Windows 95. For example, we needed the Remote Network Access ("RNA") phonebook API from Microsoft. We also needed other technical information from Microsoft, including a scripting engine in beta, and the most recent version of Windows 95. We needed to get

this data from Microsoft quickly, in order to release our retail browser product at about the same time that Microsoft launched Windows 95. We still had not received that technical information when several Microsoft employees came to our offices for a meeting on June 21, 1995.

107. Mike Homer, Andreessen, and I represented Netscape at the June 21 meeting. Rosen led the Microsoft contingent, although he was accompanied by a number of other Microsoft employees, only some of whom I remember. Marc Andreessen's notes of the meeting indicate that the other Microsoft attendees were Anthony Bay, J. Allard, Tom Reardon, Chris Jones, Barb Fox, and Richard Wolf. I remember that, for the most part, each Microsoft employee appeared to be responsible for discussing a different area of technology.
108. The discussion at the meeting covered some of the matters on which Andreessen and Rosen had previously communicated. Microsoft personnel made presentations about the various technologies that Microsoft was interested in persuading us to adopt. Mike Homer and I asked questions. Andreessen, for the most part, typed notes of the meeting on his notebook computer. Marc, who is an extraordinarily fast typist, frequently typed notes during meetings, and, on this particular occasion, I may even have asked him to take notes.
109. The technology discussions were largely unremarkable, in my recollection. I

believe there was a presentation on a security protocol Microsoft was advocating and on some Microsoft Office related technologies. I do not have any other recollection of the technology presentations.

110. The most notable thing about the meeting was something entirely different and something not covered in the proposed agenda. Microsoft's officials made it clear that they believed that Netscape should work with them on areas other than a browser for Windows 95, but that we should not develop our own browser for Windows 95 because they intended to build a Microsoft browser for the Windows 95 operating system. They proposed that a "line" be drawn between the area in which we developed products and competed and the area in which they developed products. Microsoft proposed that we build products that would run on top of the Windows 95 operating system and browser. They offered to allow us to continue to develop browsers for other operating systems, as long as we did not try to compete with them in developing a browser for the Windows 95 platform, which, of course, we all anticipated would shortly be the dominant operating system. Microsoft also proposed making an investment in our company and obtaining a board seat. Microsoft officials said that, if we agreed to the "special relationship" they proposed, Microsoft would support us by making Netscape a "preferred" ISV. The Microsoft personnel made clear that issues concerning the RNA API and related technical information we had been seeking could be resolved

“[d]epending on how we walk out of this room today.” If we agreed to the “special relationship” that they proposed, the Microsoft representatives said that we would be the first ISV to receive the technical information, mentioning that they already had an internal solution for the issue we were addressing.

111. Recognizing that our main goal for this meeting was to get access to certain code and APIs necessary for our product development, I remember asking whether obtaining those things was tied to our acceptance of this “special relationship” Microsoft had proposed, including the market division, equity investment and board seat they proposed. Microsoft’s answer was that our obtaining the necessary technical information “certainly isn’t independent” of our accepting their proposal. This fairly clear threat bothered me greatly. If we refused to agree, Microsoft made it very clear that they would attempt to crush us by attempting to own the client.
112. I have never been in a meeting in my 33-year business career in which a competitor had so blatantly implied that we should either stop competing with it or the competitor would kill us. In all my years in business, I have never heard nor experienced such an explicit proposal to divide markets. Soon after the June 21 meeting, I reviewed Andreeseen’s notes. (NET 000230-36). I did not send Marc any corrections, as would have been my practice if I had any concerns, because I believed the notes to be accurate at

the time I read them. I have reviewed them again recently. While I do not have a precise current recollection of all the details of the meeting, I do not disagree with anything in Andreessen's notes, which reflect the following assertions by Microsoft personnel:

- a. Microsoft made clear that the "set of things that are provided in Internet servers and browsers" would be "in the core operating systems or given away with the OSs as a facility like the Win32 API." What Microsoft wanted was "a partner" who would "take those core services to build on top of them and create solutions for customers." Microsoft wanted to know whether Netscape was "the kind of company that's going to partner with MS on this or not."
- b. Microsoft informed us that if we did not have a "tighter relationship" with it, Netscape would be "back to what a normal ISV can do." On the other hand, if we agreed to "a tight relationship," then Netscape could get "tight integration."
- c. Microsoft's representatives asked us whether Netscape would "be interested in a partnership where NS gets all the non-Win95 stuff and MS gets all the Win95 stuff." If we did not agree, "then that's one thing. If NS does want to, then we can have our special relationship." As Andreessen's notes make clear, we understood that to be a clear threat that "MS WILL OWN THE WIN95 CLIENT MARKET AND

THAT NETSCAPE SHOULD STAY AWAY.”

- d. When we asked about the RNA API and other technical information we needed, Microsoft’s representative said that “[w]e can fix that problem.” Microsoft admitted that there was “internal stuff that implements internal APIs, and those APIs are only known inside Microsoft.” We were told that “[d]epending on how we walk out of this room today, we have a solution for your problem.” We were told that “[i]f we had a special relationship, you [Netscape] wouldn’t be in this position.” If we did not agree to their proposal, we were told that we could not expect the APIs and other technical information for three months.
 - e. When I asked whether receipt of the APIs and other technical information was related to their proposal to divide markets and to make an equity investment in Netscape, the response from Microsoft was the “[i]t certainly isn’t independent.”
113. We rejected both Microsoft’s offer to divide markets and the remainder of their proposals. Most of the matters on which they would have had Netscape confine its work were not commercially valuable. Essentially, Microsoft was offering to allow us to work with them on matters that did not amount to much and would not have been particularly important to Netscape. In exchange, Microsoft would have obtained an equity stake in Netscape, a

board seat, and our agreement not to compete with them in the Windows 95 browser market. We simply would not and could not agree to those things.

114. Interestingly, we did not receive the APIs and other technical information we had been seeking until October 1995 -- or approximately three months later, which was well after the launch of Windows 95 and was precisely what Microsoft had threatened at the June 21 meeting.